

ECONOMIC PROBLEMS OF THE PLANNED ECONOMY

The Price System and the Allocation of Resources

W. N. Loucks and J. W. Hoot, COMPARATIVE ECONOMIC SYSTEMS, pp. 372-385

The one primary function of any economic system, regardless of its name or nature, is to produce goods for the satisfaction of human desires by the direct and indirect application of human effort to materials provided by nature.

In performing this function, a socialized, no less than a capitalistic, economy would encounter limited quantities of nature-made materials and an unlimited capacity for human wants to expand. Also, man-made producers' goods and human effort at any one time will be available only in limited quantities, in contrast with the permanent body of unsatisfied human desires. Despite whatever increases in per capita production a socialized economy may bring, it seems evident that scarcity of economic goods will have the same objective existence under socialism that it has under capitalism.

The primary operational task of a socialized economy will be just what it is under the existing economy: the guidance of the scarce agents of production into specific channels of productive use, and the restriction of effective consumer demands for specific goods to the amounts of such goods that are turned out. In a capitalistic economy this guidance, whether it be the best possible or not, is achieved mainly by permitting the willingness of consumers to spend portions of their incomes for specific products to be reflected in relatively free markets, and by permitting enterprisers to hire and organize scarce productive agents into producing units to turn out those goods the bids for which are attractive to them.

Some of the most severe and basic criticism of socialism is directed at the guidance of production which socialists propose to substitute for this free price guidance. Since socialism proposes the social ownership and operation of the means of production, goods would no longer be fed into markets by competing sellers. They would be offered for sale by various agencies representing directly or indirectly the social agencies responsible for their production. The supplies of goods thus would be marketed by what in effect would be a socially owned monopoly, the prices asked for goods and the quantities offered for sale being determined by this monopoly rather than by the freely interacting demands of many competing buyers with the offerings of many competing sellers.

It is held by some people that the decisions of these agencies controlling the flow of various goods to market, and the prices asked for them, would be arbitrarily made by the central planning bodies at the sacrifice of certain advantageous features of the existing pricing process. Moreover, these social agencies could not eliminate this arbitrary nature of the pricing process under socialism by deciding to offer all goods on the markets at their costs of production. To do this would be a no less arbitrary procedure, for under socialism there would be no competition for the two important agents of production--nature-made and man-made producers' goods. Since by the definition of socialism these would be socially owned, any values attached to them in calculating costs would be arbitrary values, placed upon them by their only possible user and owner, the social agencies involved. Thus, prices from the consumers' goods level back through the various stages of production to their origins in man's effort combined with nature would be quite arbitrarily assigned prices, not determined by the forces of supply and demand operating on competitive markets.

and set prices
or
dmts.

There is nothing innately wrong with such an arbitrary pricing of producers' and consumers' goods. The point which critics insist upon is that if such pricing takes place, consumers' freedom of choice and workers' freedom of occupational choice cannot be preserved. If goods are arbitrarily priced, either their production will have to be arbitrarily fitted to the amounts of these goods which consumers wish to take at the price set (thus requiring some direction of labor into occupational lines), or the amounts taken by consumers will have to be restricted to those quantities the social agencies see fit to produce (thus creating direct or indirect rationing). In brief, a socialistic pricing process is inconsistent with either consumers' or workers' freedom of choice, or both, and yet socialists either by assertion or by implication insist that they will preserve both of these under their new order. Certain ramifications of this inconsistency will be examined in greater detail.

Critics do not contend that this arbitrary pricing in a socialized order would have to be flavored with bad intent in order to be irrational or out of line with the totality of group well-being. By its very nature this socialistic pricing process would force those who control it to choose arbitrarily some standard or norm to which they would direct productive activity; and such a norm, by the very nature of its selection, would be irrational as compared with the automatic direction given production by a capitalistic pricing process.

Thus, it has been pointed out that such a control agency might choose to direct production along what is the most efficient line technically. In combining the agents of production, the quantities and qualities of the agents used in a producing unit might be so chosen as to achieve such "technical optima" in the organization of industry/^{that} these agencies would use more or less of a given agent in some line of production than would have been used there if the values of consumers' goods and productive agents had been determined in freely competitive markets, and enterprisers had been free to combine agents to produce goods in the most "economic" or "lowest possible cost" manner.

As soon as free market prices for consumers' goods and agents of production are abandoned as the control mechanism for guiding production, the controlling agencies are at liberty to choose any norms they like. This unrestricted range of possible choice, and the implied lack of objective determination of which norm is "best," create "irrational" and "non-economic" direction of production in contrast with the "rational economic" direction which follows from the acceptance of prices competitively determined in free markets as the controlling forces.

Some socialists have attempted to answer this charge that an objective guide to production is necessarily lacking in a socialized economy by contending that the pricing process under capitalism works so imperfectly that freely determined equilibrium prices for goods bear little, if any, resemblance to the actual price structure that has come into existence under capitalism. In fact, some socialists have been so bold as to contend that control agencies in a socialized economy can aim just as effectively at, and can accomplish more completely, those things which hypothetical competitive price equilibria are supposed to do, but actually do not do, in a capitalistic economy. A British economist has summarized this point of view as follows: "In fact, we may go so far as to say that only in a socialist community, where production can be carried on in the full light of statistical measurement and publicity, is it possible to realize the true principles of economic valuation. Capitalist society with its deviations from equilibrium due to inequalities in individual income, to competition, to monopoly, and to the mutual ignorance of enterprisers concerning other enterprisers' activities, is a very imperfect approximation of the economic ideal."

However, this is scarcely an adequate answer to the challenge that there would be an inherently less objective pricing of goods in a socialistic than in a capitalistic economy. It might be pointed out that if the socialist likes the theoretical equilibria of a competitive capitalistic economy, it would be more logical for him to follow a program of abolishing the restrictions upon the actual creation of such equilibria in the existing system than to adopt the socialist program of setting up a system in which there would be no inherent necessity of adopting similar equilibria as norms in the guidance of production.

Moreover, controlling agencies in a socialized economy could not (even if they would) choose for, and achieve in, their pricing activities norms which are the equivalents of the theoretical competitive price equilibria of a capitalistic economy. The very choice and description of such equilibria would require such comprehensive knowledge of economic phenomena on the productive and consumptive sides of the economic process as to preclude any possibility of ever establishing in a socialized economy consciously selected goals coinciding with these theoretical equilibria. Even though this were theoretically possible, attempts to do it would be completely inconsistent with those portions of socialist programs which advocate comprehensive economic planning to direct production more along lines of human needs than occurs in a capitalistic economy.

Other socialists defend a socialistic pricing process by contending that it would be possible to have sufficient competition under socialism to establish competitive values for goods in both the producers' and the consumers' goods categories. Such competitive price phenomena either would be left to guide production with some degree of automaticity or would be used by planning and pricing agencies to guide prices, production and consumption toward ends roughly corresponding to the theoretical equilibria of the existing pricing system.

A British economist has worked out such a proposal in some detail. A number of governmentally owned but semi-autonomous business units would be organized within each industry. Each of these would be substantially autonomous in selling its product and in hiring land, labor, and capital for use. In bidding for the available supplies of the agents of production, competitive prices would come to exist for each kind of each agent. Thus the concern would know how much it will cost to produce its product. Through competitive selling by these various units, prices to consumers would be kept at or near costs, and only as much as consumers would purchase at these cost-of-production prices would be turned out. Thus the prices of consumers' goods in the socialized economy would come to be equilibrium prices in much the same way as do prices in a competitive capitalistic economy. These prices, by determining the bids the producing units can make for the agents of production, would guide the various agents into their various possible uses in an objective manner, much the same as under our existing price system.

It seems obvious that such a plan is entirely inconsistent with those portions of socialist programs which advocate economic planning for the coordination of economic activity. Either producing units are to conform to a plan, or they may follow what they conceive to be the future prospective demands for the goods they produce. To advocate such autonomous producing units is a brand of socialistic eating your cake and having it which is a perfect counterpart of the proposal that comprehensive economic planning should be instituted within the capitalistic system.

This proposed method of establishing prices based on costs is, moreover, subject to a still more basic criticism. The prices of the agents of production under such a system could not be competitively determined, and consequently the unit costs of the "autonomous" producing agencies would be largely meaningless. By the very definition of socialism, producers' goods are to be socially owned. Consequently, these so-called autonomous units, in competing for their supplies of land and capital, would all be buying from the same seller. Since the supply of land is fixed by nature and would be owned socially, and since under socialism capital goods are to be created through saving by society rather than by individuals, there would be no competitive supplies of either of these agents for which the autonomous units might bid. 2. mg

There might be some possibilities of establishing competitive differentials in the prices attached to various natural resources by noting how much more the competing autonomous units would bid for the services of one piece of land than for another. But whether the general level of charges for land were to be high or low would necessarily be determined by the sole owner of these resources--the agency or agencies representing society. There is no alternative source of supply to which the producing units can transfer their demand if this owner asks "too much" (in the sense of the level of charges), and there would be no withholding of land from use if the charges for land were made low (in the sense of the level of charges). In other words, except for certain differentials in charges for various kinds of land, the sole owner, by the very nature of the situation, is forced to establish arbitrarily the level of charges for the use of land in production. The same necessity would prevail in connection with charges made upon the various autonomous producing units for the socially owned man-made producers' goods (or long-term credit) which they would need in production.

There is nothing inherently wrong with arbitrarily established land and capital charges in a socialized economy. The important point is that, when arbitrary land rents and an arbitrary interest rate enter the cost calculations of these autonomous units, the resultant per unit costs must also be proportionately arbitrary phenomena, and consequently costs and prices under such a situation are something quite different from costs and prices under a competitive capitalistic economy. It follows that when consumers contemplate their willingness or unwillingness to pay such prices, and when the productive agents are directed into various lines of use in accordance with consumer decisions based upon such costs, the resultant allotment of agents to specific uses becomes an arbitrary one, substantially shaped by the original arbitrary pricing of the two important socially owned agents--land and capital. The basically arbitrary nature of the guidance of productive agents under socialism cannot be influenced substantially by an attempt to create some "fictitious" competition under socialism. A. B. T. 15 07.11.46

The arbitrary nature of this process and its significance in the guidance of the agents of production may be seen from a simple illustration. Suppose that, in the production of commodity A, large quantities of capital as compared with land are necessary for technical reasons, whereas, in the production of commodity B, relatively large quantities of land are needed. If it were decided to place capital charges on a high level and land charges on a low level, the cost of production of commodity A would be much higher than if capital costs had been low and land costs high. Commodity B would, of course, be affected in just the opposite way. Consequently, high capital charges and low land charges would tend to make the cost of commodity B lower (other things being equal) than commodity A, while low capital charges and high land charges would tend to make the production cost of commodity A lower than that of commodity B. Thus, if one decision were made, the consumers of commodity B would be favored and more productive resources go to serve them, while,

if the other decision were made, the consumers of commodity A would be favored in the allotment of resources. This would necessarily be true despite the injection of some "competition" into the pricing process at certain stages. The necessarily arbitrary pricing, in a socialized economy, of two important productive agents--land and capital--creates substantial elements of arbitrary pricing all through a socialized price system, and this means that the allotment of productive resources to their various possible uses also is inherently substantially arbitrary.

The necessarily arbitrary nature of the pricing of the services of capital in a socialized economy should be noted particularly. In a system featured by the private ownership of capital goods, these goods will come in large part from saving done voluntarily by individuals separately, and by individuals organized corporately (through reinvestment of earnings). A supply coming primarily from such sources meets a demand for funds coming from privately owned and operated competing business units which are seeking funds for conversion into capital goods. A competitive interest rate on long-term funds results from the interaction of these two forces on investment markets. All potential savers who are induced to save by this rate will abstain from consuming certain portions of their current incomes. Thus, the division of the totality of productive energy in society, as between that used to produce consumers' goods and that used to produce producers' goods, takes place with the same automaticity and impersonality as have been noted in the general pricing processes of a capitalistic order.

Socialism transfers the administration of this saving process to society, whose planning and controlling agencies dictate the amount of social saving or capital accumulation to be done at whatever point in the economic process, and in whatever manner, they desire. No interest rate, as a function of the demand for and the supply of capital funds, any longer exists. However, individuals are free to decide to postpone consumption to the future if they care to do so. If they wish to lay aside non-perishable goods for later use, they may. Also, if they wish to save purchasing power for future use, presumably they may in a socialized economy. But since there is no longer a free investment market--socialized industry being the only agency seeking to get capital funds to use--these money savings would have to go into government bonds, savings accounts or other evidences of debt offered for sale by the financial agencies of the socialized economy.

The interest rate that such agencies would pay would necessarily be arbitrarily established, for reasons noted above. Under such a system all persons who were willing to save portions of their current income at the prevailing arbitrary rate would do so, and those who considered this rate unattractive would consume all of their current incomes. Potential savers, by adjusting their current saving activities to this arbitrary interest rate, would assist in determining how much of society's effort was to be devoted to turning out consumers' goods and how much to turning out producers' goods. But in this case the interest rate to which this response took place would in no sense be determined by those who responded (or decided not to respond). The amount of saving or capital accumulation to take place in a socialized economy necessarily must be decided upon by central agencies. There is no possible way in which individuals may be left to do this as they do in large measure in a capitalistic economy. An arbitrary raising or lowering of the interest rate obviously would bring a similarly arbitrary re-allotment of society's productive energy between its two possible uses--for the satisfaction of present desires and for the larger satisfaction of future desires.

Thus, the basic criticism of the programs of modern socialism comes to focus upon the nature of the pricing process which is inherent in a socialized economy. Such a process is practical in the sense that it could be made to work. In some ways

its operation would give an appearance of smoothness and efficiency which the capitalistic pricing process lacks. It is very probable that the socialistic pricing process also would give a certain appearance of flexibility that is lacking in the existing pricing processes. Under socialism prices could be adjusted quickly to remove from markets surpluses of goods unsalable at prevailing prices. In other cases, what would have been drastic and sudden price movements under capitalism to equate widely divergent supplies with demands, or demands with supplies, could, under socialism, be smoothed out into more moderate and gradual shifts of prices to accomplish the same ends.

The basic difficulty is that the apparent smoothness, efficiency, and flexibility of pricing under socialism are superficial. For those price adjustments which equate supplies and demands in free markets under capitalism there are substituted controlled market prices, the adjustments being forced to take place elsewhere. This "elsewhere" is primarily in the fields of consumer and occupational choices. For decisions by independently functioning consumers and workers, which decisions are reflected and coordinated in price movements in free markets, socialism substitutes price decisions made for certain socially desirable ends, but from which there follow certain necessary decisions which consumers or workers, or both, find dictated for them by the very existence of the arbitrary price decisions.

To put the matter somewhat differently, we may note that, whereas in a capitalistic economy consumers' and workers' choices are something of ultimates, shaping free market prices which control economic processes, socialism makes the chosen social ends the ultimates, setting prices on agents of production or consumers' goods, or both, to achieve these ends, leaving consumer and worker (or each person in one instance as a consumer and in another as a worker) to adapt his decisions to the chosen ultimates--the social goals. variable
independently?

From a strictly ethical point of view, it cannot be argued that starting from decisions of individuals, and letting the system respond as it will to these decisions through the pricing process, is better or worse than deciding what the system ought to do, and then dictating through the pricing process the part to be played by each individual. The vital criticism of socialism is that it insists that a socialized economy, with its necessary choice of comprehensive social goals and its arbitrary pricing to those ends, can exist without substantially interfering with either the freedom of consumers' choice or the freedom of occupational choice. If comprehensive goals are chosen, individual action must conform to them; whereas, if individual actions are left free, the comprehensive results will be determined thereby.

The advocates of real economic planning in a capitalistic order make the mistake of advocating an impossible combination of freedom of individual action and a realization of chosen comprehensive economic goals. Socialists make the same mistake when they advocate the social ownership and planned operation of our economy without interfering basically with the individual's freedom of choice. Both groups of advocates propose the impossible.

Apparently socialists either have not seen this basic issue clearly or have evaded it. It seems obvious that it is inadequate to reply to the above basic criticism by pointing out that under capitalism neither consumers nor workers are entirely free to make whatever decisions they might, in an abstract way, like to make. Thus, consumer decisions today are partially controlled by clever advertising, while occupational choices often are based upon false or ignorant ideas concerning occupational prospects. Such a contention merely confuses the issue by pointing out that the environment within which capitalism now functions imposes certain limitations upon the freedom of individual choice, whereas the socialist, by the very much

nature of his case, must deal with the inherent nature of the capitalistic system, in contrast with the inherent nature of socialism.

When the issue is put upon this plane, it becomes clear that capitalism inherently emphasizes individual choices as the directing forces in the operation of our economy, while socialism emphasizes comprehensive goals as the directing and controlling forces. It may be ethically good to have a social ownership and operation of our economy, so that these comprehensive social goals can dominate economic activity. If we are to follow the plans of socialism in this regard, we must expect a concomitant and inherently necessary modification of a certain basic freedom of individual choice prevailing under capitalism. Since this freedom, although much qualified in actual life, apparently is highly valued by many people for whom socialism proposes a new system, programs of socialism to be sound and consistent must cease to promise a continuance and enlargement of individual economic freedom under socialism, or they must demonstrate how that freedom can be preserved in a socialized economy. Modern socialism has as yet done neither.

An Alternative Approach to that of Loucks and Hoot

The pages you have just read by Loucks and Hoot present a view concerning socialist allocation which has been vigorously presented by a number of economists, among whom von Mises and von Hayek have probably been the best known. Briefly, the view is that even if a socialist government wished to follow the dictates of consumers sovereignty it would be impossible for them to do so because there is no means by which producers goods could be rationally priced. A number of eminent economists, both socialists and non-socialists, have disputed this contention. The following passage from Benjamin Lippincott reviews the answer which these economists have given to Mises and his followers. It is suggested that the student examine both of these views carefully and try to reach a conclusion regarding the validity of the respective arguments.

Two comments are suggested by this controversy which go beyond the specific issue being debated but which have important implications. The first is that even if Lippincott is correct, this does not prove that a socialist state would find it politically feasible to try to establish consumer sovereignty. Indeed, the contrary forces are obviously powerful even in a system of private ownership of productive resources. Whether these forces would be greater or weaker under social ownership is an important issue which would still have to be faced by Lippincott.

A second comment suggested by this debate is this. Clearly socialism does not by definition assume planning. Some socialists want socialism because they want centralized planning and find such planning would be unsatisfactory or impossible without socialism. Other socialists, however, like Lippincott and Lange, would prefer to place major emphasis on allocation according to consumer sovereignty as expressed through the market. The pros and cons of socialism ^{lead to mixed conclusions} except for those who can demonstrate either that Lippincott is wrong for economic reasons, or that it would be politically impossible for the socialism of Lippincott to exist.

Excerpts from Introduction by Benjamin E. Lippincott ON THE ECONOMIC
THEORY OF SOCIALISM

In the folklore of capitalism is the belief that a socialist economy is impracticable. Like many other beliefs in capitalist culture, this is widely held not only by the man in the street, but also by the economist. Of all the objections that have been raised against socialism, none have been more telling than this: that socialism cannot be worked out in practice. Men of good will might agree that a socialist state of the democratic type is superior to a capitalist on social and moral grounds, but they have given little consideration to such a state, for they have assumed that it is impracticable. If they were asked to explain their position, they would probably say two things: that socialism would not provide adequate incentives to spur men to effort, enterprise, and invention; that socialism would not be feasible economically.

None have been more responsible for the currency of this belief than the socialists themselves. Not that Marxian economists have been unaware of the problem, but they have thought about it in terms of an inadequate concept of Ricardian economics. Marxian economists since Marx have generally been dominated by the labor theory of value, with the result that they have found little or no significance in the economic tools developed by orthodox economics. Yet the irony is, as the following essays will show, that they have neglected the very thought that could have led them to an impressive technical demonstration that socialism is practicable on economic grounds.

If Marxian economists are largely responsible for failing to show how the everyday economics of socialism might be worked out in practice, socialist writers other than economists must share some of the responsibility. Writers on history, sociology, and political science like the Webbs, Tawney, and Laski have done admirable work in constructing institutions for a socialist state, but they have not pressed for an inquiry into the economics of such a state, even though the economics might vitally affect what they had constructed. They have not sufficiently considered the economic conditions that must be satisfied if a socialist state is to equal or to improve upon the standard of life provided by capitalism. Yet unless they have some understanding of the economics of a socialist state, and unless they are able to present its case on economic grounds, even though they are historians and political scientists, they can hardly hope to persuade the mass of men to believe in the state which they advocate.

It is not too much to say that orthodox economists, that is, economists of the school of Marshall and of the Austrian and Lausanne schools, are in part responsible for the poverty of thought concerning the economics of socialism. Holding that the proper field of economic theory is the field of pure abstraction, where logic and mathematics can be rigorously applied, they have limited their analysis very largely to a condition of static equilibrium--a condition where change is ruled out and economic forces are in balance. As a result of this, they have given little attention to institutional considerations. Yet the institutions they have assumed have been almost exclusively capitalist. To have assumed capitalist institutions was only natural. In the first place, they have been brought up in a capitalist economy and, broadly speaking, are members of the dominant middle class; secondly, the capitalist economy has over the years approximated in some degree to their ideal economy.

The very position of the orthodox economist has discouraged inquiry into socialist economics, which, of course, is essentially an inquiry into economic institutions peculiar to socialism. So convinced, on the one hand, has the orthodox economist been of the irrelevance of institutional considerations that he has dismissed the problem of the evolution of capitalism as a matter for mere history, though a consideration of Marx's theory of capitalist evolution might have led him to a serious examination of socialism. So attached, on the other hand, has the orthodox economist been to capitalist institutions--to private ownership of the means of production and to private enterprise--that he has not shown that his main theories would apply equally well to a capitalist and a socialist economy. Again, so attached has he been that he has not considered whether socialist institutions might permit a closer approximation to his ideal economy, though theoretically this would certainly be the case. Orthodox economists, we suggest, have given little attention to socialist economics either because they have been absorbed in the realm of pure theory or because they have been devoted to capitalist institutions.

It should be said at once that the above criticism applies to orthodox economists as a group and not to all orthodox economists, for there have been exceptions.

And now Pigou, who is one of the greatest living theoretical economists and whose very person embodies the whole Marshallian tradition, has recently come to the conclusion that a socialist economy is theoretically possible and is possible in practice, though, "extraordinarily difficult" to work out. His Socialism versus Capitalism holds that a socialist economy, on the ground of economic technique, is superior in most respects to a capitalist. It is significant, indeed, that the leader of orthodox economics has given a sympathetic exposition of socialism, in fact, has taken the position of a Fabian socialist, and has even warned against the chief danger of Fabianism. He remarks that "gradualness" is not a polite name for standing still.

Whatever may be the explanation for the widespread belief that socialism is impracticable, we are concerned here with whether or not socialism is workable from the economic angle. The problem of a socialist economy is two fold. First, will the authorities of a socialist economy dictate what products consumers shall buy or will consumers dictate to the authorities, as is the case more or less under capitalism? In more technical language, will there be free consumers' choice? Secondly, can resources be put to work so that the most will be made of them, that is, can resources be economized? In more technical language, is a rational allocation of resources possible in a socialist economy?

The first problem is, of course, easily solved; a socialist economy by definition presupposes free consumers' choice. A socialist economy in the classical sense is one that socializes production alone, as contrasted with communism, which socializes both production and consumption.

The solution of the second problem is much more difficult; in fact, the problem of a rational allocation of resources is the central problem of socialist economics. In order to solve this problem a knowledge of the relative (or comparative) importance of the primary factors of production, such as land, minerals, water power, and various kinds of labor services, is crucial. At bottom the problem of a rational allocation of resources is one of valuation, of ascertaining the relative economic significance of the primary factors of production. We must be able to value these factors, even though it cannot be done very accurately, if we are to make calculations in regard to them. Economic calculation is necessary if the most appropriate use is to be made of scarce resources.

The virtue of a competitive economy is that it makes a more or less rational allocation of resources. Under a competitive economy, the primary factors of production are valued on a market, where buyers and sellers bid with and against each other for the hire of these factors; the prices that they establish represent what all the buyers and sellers, taken together, believe the factors to be worth. These prices are economically significant, that is, they indicate the relative importance of the factors; they reflect the value placed on them by men who, under the pressure of competition, are striving to be economical in order to maximize profit. As a result of competition for profit, a competitive economy tends to do two things: to minimize costs and to make the selling price of the product equal to the cost of producing it. This tendency is the great merit of a competitive economy. Any economy that would rival a competitive one must show that there is a reasonable presumption that it will do these same two things. Otherwise there is no reason to believe that it will economize its resources.

Professor von Mises, the well-known Viennese economist and the leading opponent of socialism among economic thinkers, has argued vigorously that a rational allocation of resources is impossible in a socialist state on the ground that public ownership of the instruments of production does away with a market for capital goods. It follows for Mises that where there is no market for capital goods, there can be no prices for them; and without prices, which indicate the relative importance of the factors of production, economic calculation (or economic accounting) is out of the question.

Oskar Lange shows that Mises is able to deny the existence of prices in the capital goods industries of a socialist state by confusing the nature of prices. Lange argues that if prices are looked at not in the narrow (and ordinary) sense of the word as exchange ratios on a market (or the money for which a material thing or service can be obtained), but in the generic sense of "terms on which alternatives are offered," then there is no difficulty for socialism. For the absence of a market does not prevent the setting up of accounting prices or provisional valuations for the purpose of allocating resources.

Clearly it would not be difficult for a socialist state to set up accounting prices in the capital goods industries; the real problem is whether the accounting prices would be economically significant or quite arbitrary. Mises holds that these prices would be arbitrary--on the ground, of course, that there is no market for capital goods and therefore that the goods cannot be priced. Even G.D.H. Cole, a socialist writer, holds that accounting prices would be arbitrary.

Though Mises has been challenging the socialists since 1920, his argument had really been disproved early in the century by Barone, an Italian economist. In his notable essay, "The Ministry of Production in the Collectivist State," written in 1908, Barone proved that in principle the accounting prices of a socialist economy would be as economically significant as the market prices of a competitive economy. Though Barone indicated that it was possible to solve the calculations necessary to a rational allocation of resources in a socialist economy by a method of trial and error, he did not show how such a method could be carried out.

It was left to Taylor to point this out. The crucial problem is to determine the relative importance (what Taylor called the "effective importance") of the primary factors of production. According to Taylor, the relative importance of each primary factor is derived from and determined by the importances of the innumerable commodities which emerge from the whole complex of productive processes. The question is, how in a concrete way is the relative importance of each factor determined? Taylor's answer is that a provisional valuation, in terms of money, would be assigned to each factor. The managers of the socialist industries would then carry on their operations as if the provisional valuations were absolutely correct.

Then, if the authorities had assigned a valuation to any particular factor which was too high or too low, that fact would be disclosed in unmistakable ways. If too high an evaluation had been assigned, causing the authorities to be unduly economical in the use of that factor, a physical surplus would show at the end of the productive period. If too low an evaluation had been assigned, leading the authorities to be too lavish in the use of that factor, a deficit would show. Surplus or deficit—one or the other would result from every wrong valuation of a factor. By successive trials the correct valuation for each factor, showing its relative importance, could be found. In other words, by a method of trial and error the correct accounting price for each factor could be ascertained.

As we have said, Lange shows that a socialist economy would determine accounting prices in substantially the same way as prices are determined on a competitive market under capitalism. He does this not only by explaining that a socialist economy, like a capitalist, would use a method of trial and error, but also by pointing out that it would use this method under fundamentally the same conditions as it used under capitalism. Under capitalism, he says, the method of trial and error is based above all on what he calls the parametric function of prices, i.e., on the fact that although the prices which confront the individual business man are the result of the decisions of all individuals on the market, each individual regards the actual market prices as given data to which he has to adjust himself. Each individual business man tries to exploit the market situation which confronts him and which he cannot control.

A price structure, Lange insists, as objective or as economically significant as one under competitive capitalism can be obtained in a socialist economy if the parametric function of prices is retained. Under a socialist economy the parametric function of prices would be imposed as an accounting rule, and all decisions and all accounting of individual plant managers would be made as if prices were independent of the decisions taken. For purposes of accounting, plant managers would treat prices as constant, just as they are treated by business men under the competitive system.

We saw above the virtue of a competitive market was the tendency of business men to minimize costs in combining the factors of production and to make the selling price cover the cost of the product. How are these two things to be achieved in a socialist economy? Lange's answer is that they must be laid down as working rules, as necessary conditions under which plant managers are to carry on production.

Thus the process of price determination in a socialist economy is quite like that in a competitive one. The Central Planning Board performs the functions of the market. It establishes the same essential conditions: the parametric use of prices in accounting; and the two essential rules --minimization of costs and equality of marginal cost and selling price of the product--for combining the factors of production, for choosing the scale of output of a plant, and for determining the output of an industry. The Central Planning Board enables the socialist economy to ascertain the relative importance of the factors of production and to make a rational allocation of resources.

If much the same forces would operate a socialist system as operate the competitive, it may reasonably be asked, why change to a socialist? Lange answers this question by arguing that a socialist economy is superior in two important ways. In the first place, he says, it is superior on the ground that it could reach the right equilibrium prices (prices which balance supply and demand) by a much shorter succession of trials than a competitive market actually does. It could do this for the simple reason that the Central Planning Board would have a much wider knowledge of what is going on in the economic system as a whole than any private entrepreneur can possibly have under capitalism. As Dickinson puts it, the system would work, as it were, in a glass house in which all the details of the mechanism and its working could be followed.

With greater knowledge of the economic system as a whole, Lange continues, the Central Planning Board could more properly take into account all the alternatives sacrificed and realized in production. The most important alternatives, like life, security, and health of the workers, are, under private enterprise, sacrificed without being accounted for. A socialist economy could, on the other hand, undoubtedly go a long way toward evaluating these social costs. As a result, a socialist economy would be able to avoid much of the social waste associated with private enterprise.

Unaccounted social costs

Still more important, a socialist economy, as a result of taking into account the various alternatives, would not be subject to the fluctuations of the business cycle; at least severe depressions and great unemployment would not be likely to occur. Of course, grave mistakes would undoubtedly be made in a socialist economy, such as misdirection of investments and production; but such mistakes would not necessarily involve the whole economic system in a general shrinkage of output and unemployment of factors of production. The merit of a socialist economy is that mistakes can be localized, a partial over-production need not turn into a general one. There is no need to correct losses in one part of the economy, as is done under capitalism, by a procedure that creates in other parts still further losses by the secondary effect of a cumulative shrinkage of demand and of unemployment of the factors of production.

The second important way, continues Lange, in which a socialist economy is superior to a capitalist is in the distribution of incomes. A socialist economy, he maintains, can so distribute incomes as to maximize social welfare, while the capitalist economy that we know or are likely to know can never hope to do so. For under capitalism incomes are distributed according to the ownership of the means of production; and these are privately owned by the few, while the mass of men own

nothing but their labor power. Under such conditions, demand price (or what consumers are willing and able to pay) does not reflect the relative urgency of needs of different persons. On the contrary, it reflects the incomes of the few who go in luxury. Thus at the present time the allocation of resources as determined by the demand price offered for consumer's goods is far from attaining the maximum of social welfare.

Lange argues that if incomes are to be distributed so as to maximize the social welfare two conditions must be satisfied. First, the same demand price offered by different consumers must represent an equal urgency of need. Second, the services of labor must be apportioned among the different occupations so that the value of the marginal product of labor equals the marginal disutility involved in pursuing these occupations. In other words, that the product which results from adding the last unit of labor that just pays for itself is equal to the discomfort or pain necessary to produce it. It may appear, he says, that there is a contradiction between the first and second conditions; that the first requires the distribution of equal incomes, and the second unequal incomes. But the contradiction is only apparent. By putting such things as leisure, safety, and agreeableness of work into the utility scales of the individuals, the disutility of any occupation can be represented as an opportunity cost. An occupation offering a lower money income, and a smaller disutility, may be interpreted as the purchase of leisure, safety, and agreeableness of work at a price equal to the difference of the money income earned in that particular occupation and in others. Instead of attaching to the various occupations different incomes, the administration of a socialist economy might pay to any citizen the same money income and charge a price for the pursuit of each occupation.

There can be no doubt that a socialist economy could adequately satisfy these two conditions, whereas capitalism cannot possibly do so. A socialist economy, as Lange puts it, could base the distribution of income on the assumption that individuals have the same marginal utility curve of income, and could strike the right average in estimating the relative urgency of the needs of different persons, leaving only random errors; whereas the distribution of income in a capitalist society introduces a constant error--a class error in favor of the rich.

PROBLEMS OF THE PLANNED ECONOMY - CONTINUED

Those who advocate a planned economy as an alternative to a market economy are likely to contrast the known shortcomings of an actual order with the alleged advantages of an ideal blueprint, ignoring its possible defects. But the world has now had considerable experience with comprehensive planning, in many nations in wartime and in socialist countries in time of peace. And it is clear from this experience that such an order also has its disadvantages. The nature of some of these shortcomings may now be explored.

The principal charges that may be made against the planned economy are these:

- (1) It endangers personal freedom.
- (2) It creates new possibilities for political corruption.
- (3) It transfers responsibility for the distribution of income from the impersonal mechanism of the market to the personal pressures of politics.
- (4) It is likely to be more wasteful and less efficient than the market economy.
- (5) It is also likely to be less progressive technologically.
- (6) It is certain to create greater difficulties in international economic relationships.
- (7) And although the principal shortcoming of the market economy has been its instability, and the principal argument for the planned economy has been its promise of stability, this argument is highly dubious. These points will be discussed below in excerpts from the writings of three British economists, Meade, Wilson, and Jewkes, and the Canadian economist, Dessauer.

Planning and the Distribution of Income

In the market economy, the income of the individual will be determined by the forces of demand and supply, prices and costs. Where the consumer's demand for a good is increasing, the producer's income will rise. Where it is declining, his income will fall. Where a producer is efficient, his income will be high. Where he is inefficient, it will be low. These differences in income will leave some men worse off than others. But they will appear to these men to be the consequence of impersonal forces, not of political choice. They will therefore be accepted as a given fact, and individuals will attempt to adjust to them. Men will move out of the production of goods that are wanted less and into the production of goods that are wanted more. They will undertake to improve their efficiency. Differences in income will thus serve to direct the allocation of resources in accordance with consumer preferences.

In the planned economy, the income of the individual will be fixed by some agency of the state. The mechanism that determines it will no longer appear to him to be impersonal in character. If a man's income declines, or if it is smaller than he desires, he will feel that the government is to blame. Instead of recognizing that he is producing the wrong thing, or is inefficient, he will attribute the unsatisfactory size of his income to the policies adopted by public officials or by the party in power. And, in a democratic society, such policies are subject to change. The distribution of income will thus be influenced by political pressures. Those who are organized to exert such pressure will get larger incomes. Those who are not will get smaller ones. In the United States, we have seen how the incomes of farmers, in particular, have been increased through the exertion of political power. In the planned economy, the distribution of income as a whole will be determined in this way. Differences in income will cease to perform their proper function in guiding the allocation of resources, checking waste, and rewarding economy. Instead of shifting to the production of wanted goods, or improving their efficiency, producers will seek to increase their incomes by organizing to put pressure on the state.

So: polit. organization
big if

Planning Without Prices

J. E. Meade, PLANNING AND THE PRICE MECHANISM, pp. 5-9.

There are many persons who would wish to solve our basic problems through the formulation of a State plan giving quantitative targets for the output of each industry of any importance and for the use by these various industries of all the factors of production of any importance. Such a quantitative plan would in many cases also cover the main uses of the planned production of each industry--how much, for example, of the output of the engineering industry was to be exported, how much used for each main form of capital development at home, how much for the provision of certain durable consumers' goods, and so on. The whole plan would then be implemented by a series of State controls. Raw materials and capital goods would be allocated and licensed to achieve their planned use; labour, if the proponents of this system are both clear-headed and honest, would be directed to the planned employment; and the consumption of many, if not of all, products would be subject to rationing and licensing. Full employment and security would be achieved, since the plan would account for all available resources. Equity would be assured, since by rationing and licensing of consumption each citizen would be guaranteed a fair share of the product. The social wastes of competition would be avoided since the plan would take account of social, and not private, interests. A consistent and coherent plan would be constructed for rapidly changing conditions so that at every stage each component would dovetail into an harmonious whole.

The above is, no doubt, in many respects a caricature. But it will serve to demonstrate certain dangers and disadvantages of methods of planning which rely not upon the price mechanism but upon direct control over quantities of production and consumption. For on examination such a system is found to be not very attractive.

In the first place, the method of direct controls contains a threat to personal freedom. It is not merely that it threatens our freedom of choice as consumers, important though this is. Why, for example, should I be prevented from spending foreign exchange on foreign books or foreign travel if I am willing to spend so much less than my fair share on other imported goods or on home-produced goods which could be sold abroad for foreign currency? The pricing method (e.g., by auctioning the available supplies of foreign exchange to the highest bidder) would permit this. The method of direct controls must imply an arbitrary decision by an anonymous official as to whether I can visit my foreign friends or read their publications.

But the most dangerous threat to freedom arises from the problem of allocating labour as a factor of production among its various alternative employments. The method of the pricing system would be to allow relative wage rates to rise in those occupations in which there was a relatively high demand for labour and to decline in those occupations in which there was a relatively low demand, and to see that there was the greatest possible ease of movement from the low-paid to the high-paid occupations. The alternative, the direction of labour, is the hallmark of the Servile State; and it is a sobering observation that there appears to be at present a widespread preference for this alternative.

In the second place, a system of direct quantitative controls is the breeding ground for spivery and corruption. It is the father of black markets and carries with it an insidious threat to public morality. To make it a crime, or at least bad form, to buy in the cheapest and sell in the dearest market is to expose

every citizen every day of his life to the temptation to break the law or the recognized conventions of society. To give central and local officials the daily task of handing out, on what must inevitably be to a large extent arbitrary considerations, pieces of paper called permits or licenses of great value to the fortunate but limited number of recipients is to expose our fine and honourable public service to a strain which may in the end prove unbearable.

Thirdly, such a system of planning through direct controls involves the use of much manpower and other economic resources merely in working the controls. There can be no doubt that the system of free markets, though, of course, it involves some manpower, is much less expensive than a system of planned allocations. In this connection it is interesting to note that the number of central and local government officials increased by 700,000 between 1939 and 1947. This increase is not, of course, to be explained solely by the growth of direct economic planning. But, on the other hand, it does not take into account the effort expended by the private citizen and by private business itself in coping with the controls.

Fourthly, the method of control by the quantitative allocation of resources, quite apart from the real costs of manpower in running the controls, is bound to be clumsy, inefficient and wasteful as compared with a properly functioning price system. Take, for example, the apparently simple question whether one should plan to substitute steel for timber for a certain purpose in building. Is it economic to do so? What are the factors which the official concerned must take into account?

He must first consider the technical possibilities of substituting steel for timber in this particular use. How much more steel is required to replace a given amount of timber, and what will be the effect on the quality of the building? Unfortunately for him, the people who really know about this are not his fellow-officials but the technicians in the building industry who have a vested interest in the question and have, let us suppose, set their hearts upon getting the timber rather than the steel, because, at the arbitrary money prices fixed for steel and timber, it happens to pay them most that way.

Then there is the question where the extra steel should come from if the substitution in building is made. Should less steel be allocated for the production of cars? If so, can less steel be used per car? If so, with what effect upon the quality of the car? And what additional supplies of alternative materials will then be required by the car industry? And where should they come from? Or must the output of cars be reduced owing to lack of steel? If so, by how much? And what is the importance to the domestic economy of this country not to have less cars or to the balance of payments not to face a reduction in the export of cars? Or should it not be cars that should be affected, but a particular sort of industrial plant, or railway locomotives, or one or more of the other thousand and one end products of steel? If so, which, and to what extent, and with what further repercussions?

What, on the other hand, should be done with the timber which is saved? Should it go to railway sleepers or to packing cases? Or can it release the use of some other material in some other industry? If so, what and where are the myriad alternative possibilities, and what is the importance of each from the point of view of the welfare of our consumers, of the efficiency of our industry and of our export drive?

Perhaps, after all it would be better to produce more steel. If so, what should one give up producing in order to get the additional labour? Coal? Bricks?

One could run through a long list. But this would only shift the problems from steel to other commodities. One would not have to consider all the direct and indirect effects of reduced supplies of coal or bricks or the other commodities selected for reduced production.

Or perhaps one could import less timber and more steel. Here one may be able to reach a fairly unequivocal answer; for one can judge whether the decreased purchase of timber will save more dollars than the increased purchase of steel will cost. The firm foundation of the price mechanism at last!

In fact it is the miracle of a properly working pricing system that it will answer all these questions simultaneously, taking into account all the relevant considerations, without a centralized bureaucracy attempting to solve, without the necessary knowledge, the myriads of simultaneous equations involved. If the prices charged to domestic consumers of steel and timber bear the same relationship to each other as the prices at which steel and timber can be purchased in foreign markets, each user will, to maximize his own profit, substitute steel for timber or timber for steel if the saving in cost (and so in foreign exchange) is sufficient to compensate for any real loss in the quality of his product. If the prices of the various products which are made out of steel or other materials correspond to the costs of producing them, consumers will be induced to purchase few of the products which contain much steel, if steel is relatively scarce and therefore high in price. If the price of coal, bricks and steel all correspond to the value which the users of these commodities will place upon them--and the users will themselves take into account the possibilities of substitutes and of alternative uses--then automatically more steel and less bricks will be produced if steel is really more needed throughout its myriad uses than bricks and coal are needed through the myriad uses of bricks and coal. And the export trade will automatically be concentrated on those things which we can produce most efficiently and which have the smallest content of the scarcest, and therefore most expensive, materials.

There can be no doubt that money and the pricing system are among the greatest social inventions of mankind. Properly used they should be capable of giving each individual a general command over his fair share of the community's resources; of allowing each individual to decide for himself--where private choice is appropriate--in what form he will exercise this command; of allowing initiative to individual producers and merchants--where technical conditions permit--to produce what is most wanted, in the most economical manner, in the markets where supplies are most needed; in short, of combining freedom, efficiency and equity in social affairs.

Planning and Efficiency

Thomas Wilson, Modern Capitalism and Economic Progress, pp. 67-71

Even socialization, if it were feasible, would not, of course, provide a satisfactory solution to this problem of divided responsibility. For it would still be desirable in the interests of efficiency to delegate a good deal of authority to the managers of public corporations, and if this were done it would be unwise to make them carry out programmes prepared by central planners. If such programmes were enforced and losses were subsequently made, the managers would be in a position to blame the planners, and the planners, for their part, would be able to reply that all might have been well had the managers done their job properly. The only difference in this respect between socialism and capitalism is that under socialism all losses would be underwritten by the taxpayer, and this would be a great convenience to both managers and planners. But the inefficiency resulting from divided responsibility would still remain.

This, of course, is not the only reason why inefficiency may be expected to result from physical planning. Unfortunately it is impossible to operate controls in such a way as to permit the gradual expansion of the more efficient firms at the expense of the less efficient. The controllers may try to ensure that only so much of a certain raw material is used by a particular industry, but even in so far as they are successful this is only the first step. The total allocation has to be shared out between the different firms and these shares tend to be related to consumption at a base date or to be fixed according to some rule of thumb. No doubt an attempt is sometimes made to introduce a certain amount of discrimination, especially with regard to very large projects; but it remains true that as a rule the less efficient firm stands virtually the same chance of getting a quota as its more efficient competitor. Various criteria are applied by the controllers; but as far as the vast majority of firms are concerned, efficiency is not one of them. This is true now and it was, of course, the case during the war. Neither manpower nor raw materials were doled out with much regard to efficiency, except in the more glaring cases.

Firms operating under the rule of prices and costs are clearly in a very different position. Anyone can increase his purchases of some factor of production so long as he has the money and thinks it worth while; and there is at least a strong presumption that the firms which wish to increase their output at this cost are those which ought to do so. The efficient firm will tend to have a better profit-and-loss account and will therefore have more funds at its disposal for such purchases. To claim that the price mechanism gives an ideal result would be absurd, but common sense suggests that its defects should be analyzed and remedies sought. If some firms have what is considered to be excessive buying power, is this because the critic disapproves of the consumers' preferences which give rise to their large receipts? Or can their strong position be attributed to some monopolistic restraint and, if so, can they be made to cease and desist? At all events it is along these lines that the inquiry should be conducted; for it is scarcely sensible to reject out of hand a price system which does not give ideal scope for the efficient firm in order to substitute a regime of controls which gives far less.

That controls are defective in this way must be clearly recognized and one would have to be stubborn to the point of folly to contend that the weakness could be removed. Here, as always, the complexity of the economy must be borne in mind. It is out of the question for each controller to send his inspectors to each firm in order to investigate their efficiency--somehow defined--and no office, on receipt of such information, could hope to ration out supplies accordingly. The very inefficient might be detected readily enough and forced to close down; but such cases are rare. What is required is the gradual expansion of one firm and the gradual contraction of another; both may remain in business but their relative outputs should alter. It would be foolish to expect that controls can be operated with the flexibility and sensitivity necessary to bring this about.

The inflexibility of physical planning leads to inefficiency and delay of another kind. When production is highly specialized and divided between a bewilderingly large number of firms, it is a ticklish business for any planning authority to ensure that each one of them gets the bits and the pieces it requires in the right proportions. Furthermore, even if the plans are dovetailed with ideal accuracy on the basis of information which appears to be reliable at the time, unforeseeable developments may cause disruption. Similar mistakes are

- 6 -

bound to be made in any kind of advanced economy; but there is some reason to suppose that they will be less frequent and, above all, more easily rectified, if affairs are regulated by financial accounts rather than by remote economic planners. In a free economy, private firms will order what they want from other firms, and since the bills must be paid, they will try to order carefully. Thus "the programmes," which are only implicit in such circumstances, may well be better than those which can be prepared in Whitehall in an explicit and pseudo-scientific manner. Mistakes are always made and under both systems the firm's stock-pile may meet the need. If it fails to do so, however, it is very much easier to make good the deficiency in an economy where most things can be had at a price. A firm which needs a little more timber than was anticipated, can buy it and may be prepared if necessary to pay dear in order to get it when the alternative is to hold up production. Thus the mistake may not go unpunished; but it is the firm's profit, not the national output, which is likely to suffer most. The alternative procedure in a controlled economy is too bitterly familiar to call for any description--the form-filling, the elaborate explanations in triplicate, the administrative delays, the too frequent refusals on the part of officials who work by inflexible rules, the consequent piling up of unfinished goods and the discouragement of the worker.¹ It may be noted in passing that in such circumstances firms will tend to hoard supplies and carry bigger stocks than would be necessary under the rule of the market; such hoards are said to have reached substantial proportions in recent years. It is surely common sense to prefer a more flexible method which permits of great delegation and takes advantage of the knowledge of the men on the spot. Unless its other defects are overwhelming and irremediable, a market economy must be regarded as a much more rational alternative.

Planning and Economic Progress

F. E. Dessauer, *STABILITY*, pp. 213-215.

The possibility of progress under a comprehensive system of planned stability depends on two elements: a sufficiently strong incentive for economic progress in such an economy, and appropriate institutions to achieve progress.

The political leaders of a planned economy have three strong motives for promoting economic progress or, in other words, for improving the general welfare. One is the political necessity for raising the standards of living. This necessity does not depend on the more or less democratic structure of the community; authoritarian regimes depend almost as much as democratic ones on a state of satisfaction, or at least of optimism, which latter has also to be fed by the evidence of increased productivity. A high degree of inertia and a low state of education may detract from the aspirations of the broad masses to enjoy a better life. Enthusiasm may for some time support ascetic ideals, and the strong sense of duty may make it possible to postpone better days; still, too many people have an opportunity to compare their standards of living with those of other countries. Such feelings may have no institutional means of expression under an authoritarian regime, but dictators have an ear for the deep rumbling of dissatisfaction and they will try to appease the masses by improving their material conditions. If, however, a system of comprehensive planning is truly democratic, the desire of the masses for a better life will find its legitimate expression in parliament and public opinion;

1. The U.S.S.R., has experienced these difficulties. For example, in their book on Management in Russian Industry and Agriculture, Messrs. Bienstock, Schwarz and Yugow refer to the piling up of unfinished tractors in the famous Stalingrad Tractor Works in 1940, when the financial plan was out of alignment with the physical plan and the management lacked the small sums required to purchase the missing parts. The main factor, it may be noted, relied on 283 small and medium-sized factories which supplied 4300 kinds of machine parts. The authors have based their remarks on an article by the Chief Engineer of the Stalingrad Tractor Works which appeared in Pravda, October 27, 1940.

this will lead to the formulation of an economic policy which aims at higher production for higher consumption.

Planned economies are experiments. Of recent origin and lacking the support of custom and experience, they feel, sometimes in a rather juvenile way, that it is necessary to prove their equal efficiency and progressiveness to the still undecided observers at home and abroad. If the planned economy is authoritarian, the leaders will be sensitive to accusations of violent rule or illegitimate origin, and there is no better defense against this reproach than positive accomplishments in the service of the masses. This too will suggest to the leaders the promotion of economic progress, and especially those forms of progress which are open to statistical proof. Authoritarian systems are, as a rule, aware of what the demonstrations of their greatness and efficiency contribute to their political strength, and there are few more impressive manifestations of this fact than new power dams or streamlined locomotives of a state-owned railway or the long, uniform fronts of new factory buildings, with bright workshops and clean eating rooms for the workers.

But the strongest motive for industrial progress, much stronger in authoritarian and in the more radical socialist systems than in liberal ones, is the fear of war, the deep consciousness of the chaos of the world, and the constant awareness, lacking in the rational minds of most liberals, of the irrational nature of man and of the tragic character of political conflicts. Preparation for war and for victory is today the most powerful incentive for industrialization, but what has been invented and created in order to destroy serves, later on, to increase productivity and to improve the standards of living. It is easy to condemn such preparations with moral or even with legal arguments. There are, in fact, wars of aggression without any moral or political excuse; but there are many more cases where in our search for the subtle distinction between aggressive and defensive war we get lost in the jungle of causality. The fact is that many nations, not by hereditary disposition but as a result of their history, are inclined to take a rather pessimistic view regarding the good intentions of their neighbors and the general harmony of interests. These sentiments exist and are understandable; whether or not they are justified is of little importance. Nations which are of this state of mind feel always "encircled" and threatened; they will prepare weapons which, in the actual state of technology, comprehend the whole sphere of industrial production.

The result is that in authoritarian and socialist systems the incentives for economic progress are at least as strong as in the liberal economy, and certainly as strong as under a controlled, rationalized, and slow-moving capitalism. These incentives, in order to be effective, need the support of appropriate institutional devices. The capitalistic economy developed a system of economic rewards for progress and punishments for inertia which, in their actual forms, do not fit into a socialist order. But systems of planning can develop their own methods of reward and punishment which may work as well as the capitalistic ones. Instead of a competitive market the regular comparison between similar factories, services, and offices can measure efficiency and stimulate progress. As long as criticism is allowed or even invited, the consuming public can watch over the quality of products and the efficiency of services and assist by this check the supervision by the government. The ambitions of engineers and chemists, managers and workers to improve their achievements and to show their craftsmanship operate independently of the economic system. No authoritarian government lacks the means to honor and to reward the efficient and to punish the inefficient. The application of new

inventions and innovations does not meet any inherent difficulties as long as the planning committee feels the need for economic progress under the pressure of the stimulating motives mentioned above. The pace of progress may be slowed down, but the dynamic force of individual ambition and economic liberty can be equaled under certain political conditions by the driving power of the government, at least for some time.

John Jewkes, ORDEAL BY PLANNING, pp. 171-178

The causes of the growing faith throughout the world in the benefits of a centrally directed economic system are numerous and complex, but one is undoubtedly the belief that only through detailed central planning can stability and security be provided. The lure of balance and order in our economic arrangements is proving irresistible even to many people of deep liberal instincts who recognize some of the social and political dangers of regimentation but who are so desperately anxious that men should be masters of their economic destiny that they are prepared to delegate to politicians control over the means of production and over the freedom of consumers. They may have doubts as to whether the State will be a competent receiver, but shuddering at the boggy of chaotic competition and ignorance of the working of the price system in a free economy, they close their eyes and plunge for the plan.

Many writers, notably A.G.B. Fisher in his Economic Progress and Social Security, have shown conclusively that rapid economic expansion cannot be expected if the claims for individual security are pressed unduly and that some economic untidiness is the price we must pay for the general gains of economic progress. The thesis of this chapter is a rather different one. It is that the centrally directed economy must inevitably tend to wasteful discontinuity and disruption in the process of production. The outward manifestations of such waste can often be concealed. The waste of labour need not result in open unemployment. It may simply mean under-employment, hoarding of labour and the performance of useless tasks. Or it may be cloaked by imposing slavery on the individual worker, by savagely bustling him about from one occupation to another with little regard for his convenience, aptitudes and inclinations. On other occasions, however, the dislocations may be so great as to defy concealment. Planning 'crises' supervene in which violent upheavals are called for in order to 're-balance' the economy, and in which the enthusiasm of the Supreme Planners to discover and punish the scapegoats is matched only by their anxiety to find alibis for themselves.

What does the planner mean by economic stability? What is it that is to be stabilized: income, prices, profits, money wages, real wages, employment, output, the distribution of income, the technical methods of production or all or some combination of these? And what is implied by stability: a complete absence of change, a constant rate of change upwards, or simply the absence of any change which the community itself has not arranged and ordered? One striking paradox is evident at the outset. When the planner demands a stable economy he is not asking for a stationary society. He wants wealth to increase, industries to be progressive, population and the labour force to grow. He wants rapid change and progress as well as stability. He wants his bread buttered on both sides. Unfortunately for him, and for the rest of the world, the methods he proposes to employ must prevent him from having it even on one side.

(VALUES IGNORED)

Why must a centrally directed economy inevitably prove highly unstable? First for political reasons. So long as the community claims to be democratic then it must retain its powers to change its government. When a government pledged to planning is superseded by one which favours the free economy, the changeover will involve surgical operations on industry, the actual performance of which must weaken, and the very prospect of which must partially paralyse, the process of risk-taking and the exercise of forethought in industrial operations. The present position in Great Britain provides a good illustration of this. The Conservative Party is committed to the reversal of certain schemes of nationalisation already carried out by the Labour Government in their first term of office. The Conservatives would almost certainly be compelled, if they ultimately came back to power, to restore the free economy in those further sectors which the Labour Party has in mind for nationalisation if given a second term of office. Long-term industrial projects cannot flourish in such an environment of political uncertainty any more than can sober living among those persons who expect every day to be their last.

Even where one planning government is succeeded by another, sudden switches of policy are to be expected. For where the rival parties all subscribe to the idea of a directed economy they will compete for the claims of the electorate by different views of the would-be Supreme Planners as to the correct distribution of national production between consumption and investment, home consumption and export, essential and inessential industries. The prospect is thus opened up of chaotic competition between rival plans. There is no escape from such a dilemma unless one party has the courage of its convictions, and in the interests of the continuity of its economic programmes, deprives the electorate of the right to change the government. chaotic?

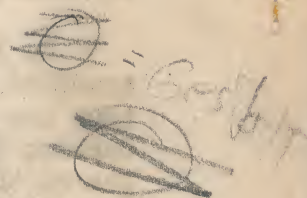
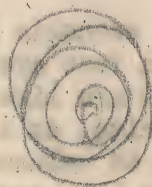
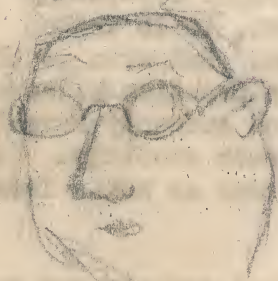
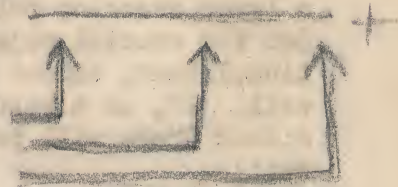
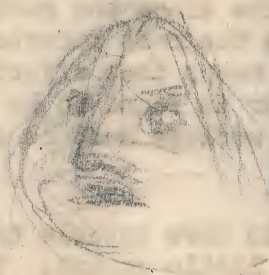
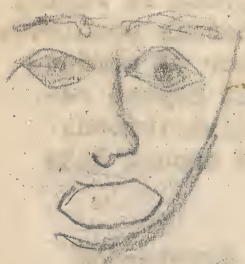
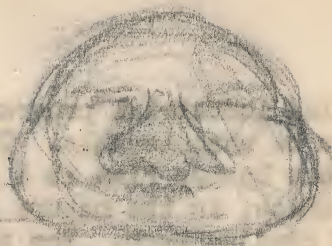
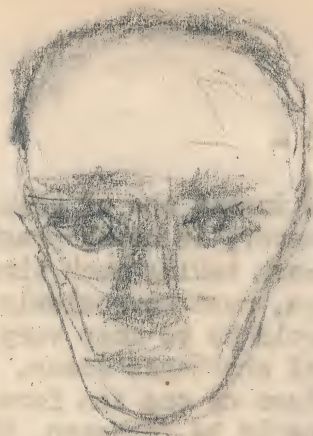
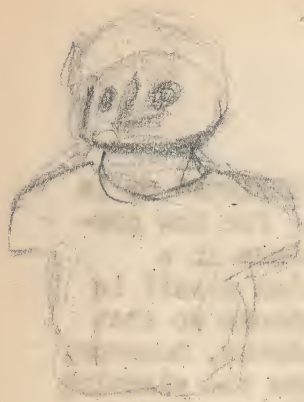
A centrally directed economy is subject to the full impact of political instabilities. But these are no more dangerous than its inherent tendency to create confusions for itself and to pass from one production crisis to another. The point can be most easily explained by considering the nature of the production programmes which, in the planned economy, must be laid down for each industry and each firm. The absence, in such a system, of the more normal incentives makes the achievement of the programme one of the main incentives--it is upon the comparison of actual output with planned output that workers and managers must be rewarded or punished. So long as the Supreme Planners are pressing for the maximum industrial production they are bound to raise all the integrated programmes of the different industries to a level which will keep the system as a whole at full stretch. The carrot must be dangled so nicely in front of the nose of the donkey that he will never lose hope of reward, but never be allowed to attain it without putting forth his maximum effort.

In a system in which there are many thousands of programmes this inevitably means that some of the programmes will not be achieved. Since they are, in any case, guesses which are just as likely to be wrong as right, and since, in addition, they are infused with a strong element of wishful thinking, only by a miracle could they all be just achieved and no more than achieved. If one programme is not achieved all other programmes are thrown out of balance and waste and unemployment result. If the steel output is not achieved, then some machine tools which should have been produced cannot be made for lack of raw materials. Some labour in the machine-tool industry will then be unemployed. If the machine-tool programme is not achieved then some industries will be short of machine tools and their production will fall short of the target. General disequilibrium will result. If the programme for railway-wagon wheels is not reached then there will be a shortage of wagons with the consequent effect throughout industry. There are only two possible ways out of this dilemma. The first would be to change the whole

of the detailed industrial programmes the moment one of them is not achieved or is recognized to be unachievable. That, however, is never practicable. For the preparation of the Master Plan is a mighty work taking much time and labour in a bureaucracy which, in the nature of things, must move slowly. The plan itself is the enemy of readjustment. The second would be to keep very large stocks so that mistakes could be rectified before crucial shortages occur. These stocks, however, would have to be stocks of everything--since no one can forecast where the planning mistakes will be made. If the mistakes could be foreseen, they could be avoided. The maintenance of such stocks is itself a confession of weakness, goods in store are temporarily lost to the community. Moreover, when technical progress is rapid, a large stocking policy may lead to sheer waste since the goods may become obsolete. But the crucial objection to stocking is that the most important factor of production, labour, cannot be stocked: unemployment means that effort is lost beyond recall. If, as a result of bad planning, labour is found to be badly distributed, either there will be under-employment or the workers must be switched around like cattle.

If the plan and all its constituent parts were capable of rapid day-to-day readjustments, original failures would be of little moment. That, it is argued above, is impossible because of the intricate nature of the plan. But even if this were theoretically possible, it would still remain impossible in practice because impending break-downs will be concealed up to the last moment and suddenly revealed only when it is too late for the economic system to turn the corner smoothly. It is characteristic of all planned economies that policy changes come as bolts from the blue.

So long as the vast economic blunders of a centrally directed economy are not accepted for what they in fact are--the logical results of the planning process--then the remedies applied are likely to magnify the original errors. For the Supreme Planners will strive, as a first line of defense, to make a positive virtue of their failure and to welcome the economic vicissitudes to which they have exposed the people. They then argue that the best way to keep the economic system moving smartly along is to adhere to the plan, watch for shortages as they arise and deal with these shortages as quickly as possible. This is the policy popularly known as creating a vacuum, pushing hard all along the production line and hoping for the best. It explains why a planned economy is always in some sort of a crisis, why there is always a 'battle' going on for something. Special efforts are flung into the economic system at the point of weakness. This, however, can only heighten the confusion and waste of the system as a whole. For special efforts can only be efforts outside the plan, they really amount to scrapping the plan without openly admitting it. Frantic last-minute scrambles to repair the breaches naturally play havoc with the disposition of the other factors of production in the economy. The confusion is spread far and wide.



DADY

